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**Booming Pandora struggles to win over advertisers**

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Pandora Media's online music service is the most downloaded free music program in the Apple and Google app stores. It draws more listeners in New York and Los Angeles than the largest radio stations in those cities.

And yet, Pandora's dominance hasn't won over traditional radio advertisers, which are wary about buying ads on phones and tablets. While more than 70 percent of Pandora's usage happens on mobile devices, less than 1 percent of overall U.S. advertising spending is devoted to that market.

The slow adoption is making it difficult for Oakland's Pandora to reach profitability - something that won't happen until fiscal 2014, analysts estimate. The company also faces mounting competition from music-streaming services Rdio of San Francisco, Last.fm and Spotify. The woes have contributed to a 16 percent decline in Pandora's stock since its June initial public offering.

"They just can't sell advertising that fast," said Mark Mahaney, an analyst at Citigroup in San Francisco. Users are "shifting so rapidly towards mobile devices, and it's going to take longer for the monetization to pick up."

In terms of listeners, the company is expected to continue its rapid expansion. The service, which had 23 million active users in 2010, is projected to grow 21 percent annually and reach 159 million active listeners worldwide by 2020, said Scott Devitt, an analyst at Morgan Stanley.

The mobile service has struggled to attract advertising in part because Pandora is creating new types of ads, blending 15-second audio clips, display ads and video spots. Audio ads on the radio have traditionally been directed to local audiences, while display advertisers are more often national brands. Pandora's service is multimedia and focused on national and local advertisers, an experiment that most companies aren't used to.

The company also doesn't have enough sales representatives to keep up with user growth, and in cities like Miami and Atlanta, it has no salespeople, said Chief Financial Officer Steve Cakebread.

"It's really tough to grow our sales organization 125 percent year-over-year," Cakebread said at a Goldman Sachs Group conference last month.

In cities where Pandora has sales offices - including San Francisco, New York and Los Angeles - the company already averages more time with listeners than the biggest local radio stations, Devitt said, citing company estimates and data from Arbitron, a radio researcher.

Meanwhile, Pandora is subsidizing its mobile business by bolstering advertising on its website. Last month, it added new features including video commercials that command higher rates from advertisers compared with audio spots, Cakebread said. Revenue from Pandora listeners using computers is nine times higher per hour than from those on mobile devices, Devitt estimates.

Along with the site redesign, the company lifted a 40-hour cap on computer listening, which had forced users to pay for a premium service if they exceeded that number. Previously, when the cap was reached, users would switch to listening on mobile devices. All listening is now free and ad-supported, a change that may add $53 million in revenue in the next four years, Devitt said in a Sept. 23 report.

The company needs that extra cash to deal with another challenge - a growing field of rivals. Clear Channel Communications, the largest owner of U.S. radio stations, jump-started its iHeartRadio Internet offering last month with a series of concerts in Las Vegas. The service, available online and through applications on mobile devices, lets listeners create personalized playlists and listen to its broadcast outlets.

Pandora also faces new competition for listeners' time from Spotify, operator of Europe's biggest online music service, which began signing up U.S. customers for its ad-supported and subscription plans in July. There's also Rdio, started by a co-founder of Skype Technologies, which began offering free music without advertising this month.

Pandora should be able to ward off fee-based rivals, because it has a vast music portfolio and a loyal audience, said Mahaney, who recommends buying the stock.

"You'd have to have a dramatically better mousetrap for somebody to switch away from a free service to a $10-a-month service," Mahaney said. "The end market is a lot bigger for an advertising-supported model than for a subscription-supported model."

Morgan Stanley's Devitt agrees that it's just a matter of time before ad dollars follow the users. Mobile revenue for each hour of music provided to listeners will almost double to $40 in 2016, topping the rising costs Pandora pays the record labels to license music, Devitt estimates. He says licensing fees will climb 35 percent to $23 an hour.

Advertising on mobile devices is expected to jump almost twelvefold from last year to $10.5 billion in 2015, compared with a 32 percent rise in overall U.S. ad sales to $328.6 billion, according to IDC data. Pandora is preparing for that surge by putting its service in front of as many music lovers as possible, even if it's a currently a money-losing endeavor.

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